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Investec Property Fund Limited

South Africa Corporate Analysis **July 2013**

Security class	Rating scale	Rating	Rating outlook	Review date
Long term	National	A- (ZA)	Stable	July 2014
Short term	National	A1-(ZA)		

Financial data:

(US$'m Comparative)

	31/03/12	30/03/13
R/US$ (avg)	7.46	8.50
R/US$ (close)	7.69	9.24
Total assets	270.7	502.1
Total debt	17.0	48.7
Total capital†	239.0	426.8
Cash & equiv.	0.6	43.2
Turnover	32.4	44.1
EBITDA	25.7	34.7
NPAT	0.0	0.0
Op. cash flow	23.3	26.8
Market cap*	US$507.7m	
Market share	n.a	

*As at 23 July 2013, @ R9.80/US$.

† Includes subordinated debentures.

Rating history:

Initial Rating (11/2011)
Long term: BBB+(ZA)
Short term: A2(ZA)
Outlook: Stable

Last Rating (11/2012)
Long term: A-(ZA)
Short term: A1-(ZA)
Outlook: Stable

Related methodologies/research:

Criteria for Rating Corporate Entities
Criteria for Rating Property Funds
Investec Property Fund Limited ("IPF") Rating Reports, 2011-2012
IPF R450m Senior Secured Notes: New Issuance/Surveillance Reports, 2012-2013

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Summary rating rationale

The ratings are based on the following key factors:

- Strong capital support derived from parent Investec Limited ("Investec") is a key underpin to the rating. Planned enhancement of scale should see IPF closely aligned to larger, more established funds in the medium term. Although cognisance is taken of mitigants employed by the fund, rapid acquisitive growth elevates investment risk, especially given the upward pressure on capital values within certain market segments, as several funds also seek to expand.
- While IPF's limited track record remains a constraint to the rating, linkages within the Investec stable and management's strong real estate credentials serve as mitigating factors. This has been borne out by IPF successfully ramping up scale within a relatively short time frame, leveraging group synergies and long standing business relationships with Investec Bank clients.
- The high quality pool of real estate assets evidences long term leases and low vacancy levels. This has ensured strong cash flows, underpinned by sound escalations and reversions. As such, margins remain robust despite the increased retail exposure, and should support comfortable medium term debt serviceability.
- Concentration risk has reduced as the fund has attained scale, with 55% of the portfolio's carrying value at FYE13 derived from 10 properties (FYE12: 75%). Single-tenanted properties contributed around 55% of revenue (FYE12: 58%), and this helps to manage down the fund's cost to income ratio. The maintenance of a chiefly A-graded tenant profile also mitigates counterparty risk.
- Gearing levels remain very low, and management does not anticipate that the LTV ratio will exceed 30%-35% in the short to medium term. This compares favourably to a 40% benchmark for highly rated property groups.
- The R3bn DMTN programme provides access to capital markets, while liquidity is underpinned by a R500m bridging facility. Close relationships with bankers should enable IPF to successfully secure other funding facilities, further improving financial flexibility. This is supported by the low percentage of encumbered properties (FYE13: 23%), implying strong recoveries for potential unsecured note holders.

What could trigger a rating action

Positive movement factors: Upward rating pressure would result from a strong medium term performance track record, underlined by the positive earnings impact of new acquisitions.

Negative movement factors: Materially higher than projected gearing metrics, driven by deteriorating market fundamentals or unanticipated investment risks, could place downward pressure on the rating. In addition, a material reduction in Investec's shareholding would have a negative impact on the rating.

Business profile and recent developments

IPF was listed on the JSE in April 2011, initially as a limited liability property loan stock company ("PLS") with a mandate to procure and manage income generative office, retail and industrial properties with upside potential. IPF was dormant until its listing, upon which it acquired 29 assets from parent Investec. Largely through acquisitive growth, IPF intends to increase the value of its real estate assets to approximately R8bn-R10bn in the medium term. As at FYE13, Investec and Investec Asset Management together held 54.01% of the fund's linked debentures. Management holds a nominal proportion of issued and outstanding linked units, and the remainder is mostly controlled by various institutional investors.

IPF's Real Estate Investment Trust ("REIT") status became effective from April 2013. In this regard, a conversion to an all-equity structure was proposed in a July 2013 circular to linked unitholders. This will be achieved by delinking debentures and ordinary shares, and capitalising the value of the debentures to the stated capital account. Par value shares will also be converted to ordinary shares of no par value. The debenture trust deed will be amended to enable the conversion, and will ultimately be terminated, while the memorandum of incorporation will also be amended to incorporate the conversion. Linked unitholders are expected to pass resolutions that will facilitate these changes in general meetings earmarked for the 16th of August 2013, with the conversion to be finalised by the end of September.

IPF purchases quality assets with a high-grade tenant profile. The fund does not take on development risk, either through greenfield projects or properties that require major renovations. Although IPF's portfolio has a number of small, mostly industrial properties, it is focused on medium to large transactions. This has been borne out by the value of deals made in F13 and into F14, which ranged between R60m-R300m. Nonetheles, smaller assets may be purchased as part of a larger, competitively priced or positioned portfolio, or if they are strategically adjacent to other Investec properties. Management does not plan to invest in an equity portfolio, although on occasion, linked units in other funds may be procured in the process of disposing of assets, where consideration is in the form of equity.

Acquisitions are usually timed in a way that enables IPF to minimise the cost of procurement or to secure cost effective financing. The fund does not purchase its properties piecemeal, and it does not co-own buildings or partner on acquisitions with other entities. This improves its flexibility, especially in instances where properties may be required as collateral, and gives management full oversight and control of its operations.

Investec Property Proprietary Limited ("Investec Property") is the appointed manager of the fund. The parties have a 7-year asset and property management agreement that may be terminated on 6 months' notice. Tasked with the fund's property asset management, Investec Property identifies investment opportunities for IPF and is also responsible for securing the requisite funding to finance acquisitions. The day-to-day maintenance and general administration of properties is outsourced to reputable property managers. In this regard, the fund relies on its management team's strong real estate credentials, long standing relationships with property managers and extensive experience derived from having established other large property funds. Rigorous internal due diligence processes, credit score cards and extensive client lists provide competitive advantages over similar-sized funds, especially in terms of potential acquisitions.

In March 2013, IPF entered into agreements to procure 5 single-tenanted properties for a total cost of R318m. Two of the properties were purchased from Investec Property Limited, at a cost of R193m. The acquisitions were funded by existing cash, and as such, the fund's debt levels remain unchanged. This, however, could change materially in the short term, given IPF's aggressive growth mandate.

Post F13 year-end acquisitions (R'm)	GLA (m^2)	Purchase price	Independent valuation	Yield %
5 Bond Street	5,870	118.4	119.0	8.4
SA Ladder Blg	25,000	75.0	75.4	10.2
BMW Auto Alpina	7,526	63.4	-	9.5
Minolta Properties	5,121	60.8	-	8.8

Having raised R1.5bn through a rights offer and R450m from the DMTN programme, IPF made acquisitions worth R2.1bn during F13. The balance was settled by an issue of 34m linked units to Giuricich and Investec. The fund continues to explore various acquisitive opportunities, leveraging its ready access to liquidity and flexible funding options. Management has, however, emphasised that its strict procurement criteria remains in force. As such, the timing of potential purchases or the size of new deals remains highly uncertain, and is predicated on the availability of quality real estate that is a strategic fit for the fund. IPF has a long term view towards its assets, and rarely disposes of properties. Exceptions nonetheless arise when smaller assets that are misaligned to the fund are procured as a part of a fund or pool of properties. Since March 2012, IPF has sold 3 non-core properties for a consideration of R280m, deriving a profit of R48m from the disposals.

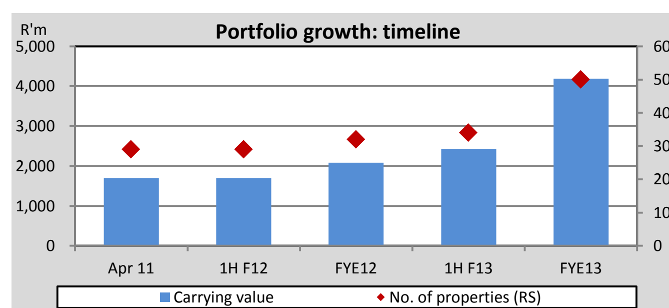
Acquisitions, F13	Cost (R'm)	GLA (000s m^2)
Office	**442.3**	**20.1**
The Firs	272.3	13.8
Investec offices Pretoria	170.0	6.3
Industrial	**119.1**	**11.2**
GE Property	119.1	11.2
Retail	**1,547.8**	**159.0**
Giuricich portfolio*	742.8	70.8
Balfour Park	295.8	36.3
Megamark Mall	202.3	23.1
Great North Rd Plaza	145.0	13.5
Other	161.9	15.3
Total	**2,109.2**	**190.3**

*Consisted of 12 properties.

Property portfolio

As at March 2013, the portfolio had doubled in size in comparison to the FYE12 position. It consisted of 50 properties, from just 29 at its inception. This saw the fund's combined GLA rise by 40% to 568,151m^2. The carrying value also rose to R4.2bn (FYE12: R2.1bn), underpinned by the Giuricich, Balfour Park and The Firs acquisitions during the year. Independent property valuations are carried out at year end by an accredited

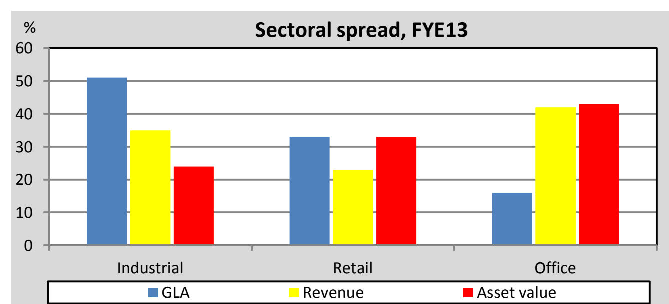
external valuer, and are conducted on a rotational basis to ensure that each property is independently assessed every 3 years. Unless otherwise stated, the following analysis is primarily based on the fundamentals of properties held as at March 2013.



The enhanced scale has seen the top 10 properties account for a lower 55% of the total portfolio's carrying value, from 75% at FYE13. The 10 largest contributors to rental income also accounted for a reduced 52% of total turnover in F13. This is in stark contrast to a 92% revenue contribution derived from the top 10 assets in the much smaller original property pool.

Top ten properties, FYE13 (R'm)	Carrying value	% of portfolio	
		By value	By area
Woolworths House	319.0	7.6	5.4
The Firs	305.0	7.3	2.4
Balfour Park Shopping Centre	296.0	7.1	6.4
Alrode Multipark	274.2	6.5	16.0
Investec Offices Durban	232.0	5.5	1.1
Megamark Mall	213.7	5.1	3.7
Innovation Group	190.0	4.5	2.7
Investec Offices Pretoria	173.4	4.1	1.1
Great North Rd Plaza	157.0	3.7	2.3
Builders W/H The Glen	139.0	3.3	1.9
Total	**2,299.3**	**54.9**	**43.2**

Geographic concentration, however, remains high, with Gauteng properties contributing 67% of rental income and constituting 72% of the fund's GLA. Western Cape and KZN properties held at FYE13 made a 14% and 9% contribution to rental income respectively. IPF does not actively manage geographic or sector diversification. Instead, the focus is on securing quality acquisitions with strong underlying property fundamentals and stable revenue streams. Nevertheless, management plans to increase its footprint in certain provinces over the medium term.

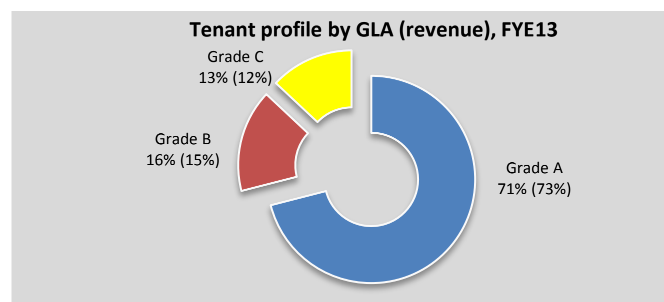


As planned, the retail segment has been augmented by strategic asset purchases, to account for 33% total GLA and 23% of revenue at FYE13, from a respective 9% and 10% derived from the original pool of retail assets. The top 5 properties equated to 54% of the retail assets' carrying value, and made up 22% of the total portfolio value. Retail assets accounted for R1.5bn of acquisitions made during F13. IPF largely targets prime-located, 'big-box' retail properties that attract top-end, A-grade tenancies. These properties evidence fairly income inelastic demand, insulating the fund from the impact of constricted consumer spending. The portfolio also has strategically located retail centres that cater for the expanding mid-LSM market.

Office properties made the largest contribution to the total portfolio's carrying value and rental income, at 43% and 42% respectively. The segment consists of just 8 properties, with the top 5 making up 81% of the total value. The quality of assets is such that the majority are A-grade tenanted, including multi-tenanted properties such as The Firs. With the exception of 230 15th Road, all office properties were fully let.

Albeit comprised of 22 properties, industrial evidenced material concentration, with the top 5 assets accounting for 63% of its carrying value. This is because the fund holds a number of small to medium sized, largely single tenanted industrial properties, whose asset values range from R7.8m to around R30m. In terms of the total portfolio, the sector's contribution by value and revenue equated to a respective 24% and 35%. The segment is anchored by Alrode Multipark, whose carrying value of R274m as at FYE13 has been augmented by cumulative fair value gains of R86m since April 2011.

A-grade tenants, comprised of large national or listed companies, government departments as well as major franchisees, contributed a higher 73% of rental income (FYE12: 62%). Notwithstanding the fund's broader sectoral diversification, management's focus on high-grade properties should result in the maintenance of a predominantly A-grade tenanted property portfolio. The split between B and C-grade tenants' contribution to revenue is relatively even. C-grade tenants currently only occupy industrial space, with IPF having disposed of its 2 C-grade office properties during F13.

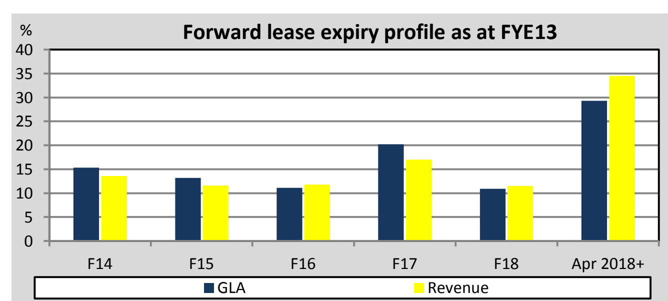


A secondary consequence of the broader diversification by sector has been a moderate reduction of the contribution of single tenanted properties to 55% of rental income (FYE12: 58%). Single tenancies are central to the efficacy of IPF's operating model. As tenants sign mostly long term, triple net leases, this is supportive of its atypically low cost to income ratio. In addition, management typically secures renewals on such leases well ahead of their expiry dates, usually with strong reversions in evidence.

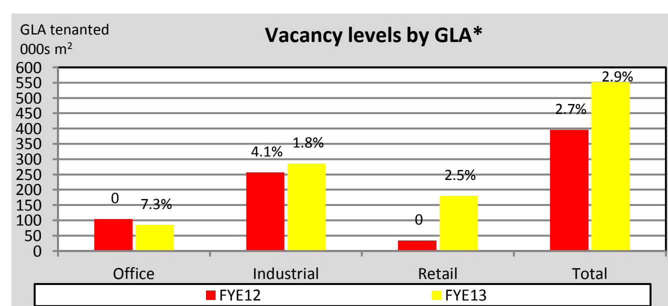
The relatively smaller client base (in comparison to a fund largely reliant on multiple-tenanted properties) implies increased concentration and counterparty risk. In this regard, a client defaulting, as well as the non-renewal or early termination of a lease would drive a drop in occupancies, resulting in an unanticipated fall in

cash flows. To mitigate this risk, triple net leases are only accorded to high quality tenants that are strictly vetted, employing Investec Bank's credit score cards. Stringent due diligence processes are also conducted, especially when single-tenanted properties with long term leases are being considered for purchase. Office and high-grade industrial space typically attracts single tenancies. On the other hand, a national, A-grade retail client can take up space across various properties. Nonetheless, no single tenant accounts for over 7.6% of rental income.

Long dated leases of up to 10 years account for well over 90% of IPF's rental income. The balance is derived from assumed renewals, as well as newly let properties. In terms of both revenues receivable and GLA, the fund maintains a well-spread forward lease maturity profile, with 11%-17% of leases expiring in each of the 5 years to F18, and around a third thereafter. This is in line with the 15% annual expiry benchmark for highly rated funds. The average tenure of triple net leases is close to 10 years, while overall, contract renewals are usually for a period of at least 5 years. Although the portfolio has grown rapidly, long lease maturities have been secured across new acquisitions. This has enabled IPF to improve its lease expiry profile.



The fund achieved above inflation rental escalations on existing leases of 8.9%, approximating an average escalation of 9.2% reported on a smaller portfolio in F12. The vacancy level remained low, at 2.9% (F12: 2.7%), and was largely attributed to the non-renewal of a single-tenant lease in a small office building. This temporarily raised office vacancy levels to 7% by year end. Minor vacancies at new acquisitions Megamark Mall and Balfour Park also contributed to the nominal increase in overall vacancies. As this was priced into their acquisition, however, the fund did not have to pay for the vacant space. It is likely that vacancy levels will rise moderately with new acquisitions. Nonetheless, overall occupancy levels are expected to remain well above industry norms going forward. This is because IPF does not purchase assets with high vacancies (although levels may fluctuate intermittently).



*Labels indicate vacancy levels per sector.

Operating environment

Real GDP growth remains constrained, and is expected to register at a lower 2% in 2013 (2012: 2.5%), in view of elevated sovereign risk, weakening macroeconomic fundamentals and the impact of protracted labour related stoppages in mining and agriculture. To counter the adverse impact of a slowing global economy and stimulate growth, domestic monetary policy remains accommodating, with the repo rate unchanged since the last 50b.p. reduction to 5% in July 2012. Together with higher disposable income and a sharp rise in unsecured lending, this notably boosted consumer spending.

This surge in consumer confidence and improved liquidity derived from greater access to capital markets and rising corporate lending largely supported property sector recovery. As such, the market capitalisation of listed property funds has ballooned from R5bn in 2001 to over R200bn, as investors chased a combination of yield and certainty of return. Prime grade office space, where IPF primarily operates, has evidenced strong occupancies and lease reversions. New developments are, however, primarily tenant-driven and this has served to further shore up demand for A-grade space. The B-grade space remains considerably pressured, with vacancies expected to remain above historic lows until stronger economic growth ensues. In contrast, industrial occupancies and rental escalations continue to improve despite subdued manufacturing performance. Upward pressure on capital values is also in evidence, especially in strategic locations. Looking ahead, a strong development pipeline for industrial space is likely over the medium to longer term. This, however, is predicated on sustained recovery in the underlying secondary sector.

Retail sales have been fairly sound in recent years, registering real growth of 5% in 2012 (2011: 6%). This has insulated sections of the retail property segment from the vagaries of the domestic environment. Funds with the requisite scale have accordingly established medium-large shopping centres in outlying districts such as townships and rural areas, with an additional 600,000m^2 of retail space expected to come online by the end of 2014. National retailers have been expanding their geographic footprint, boosting demand for space in these areas. The operating environment for commercial retail real estate in urban areas is, however, much more challenging. Changing space requirements, cautious corporate spend and liquidations of SMEs in the highly uncertain economic environment have resulted in reduced renewals and high vacancies. The dominant positioning and upmarket nature of IPF's retail centres currently provides protection from rising competitive pressures. Nonetheless, a rapid rise in retail space will impact industry performance should the economy continue to weaken.

Overall, cannibalisation of smaller property funds is likely, as well funded groups seek to enhance scale. In addition, slowing consumer spend is evidenced by constrained retail sales statistics. Earnings pressure will also derive from planned electricity tariff hikes. With

municipalities effecting reviewed valuations and other changes with a view to overhauling revenue collection, margin compression is expected in the medium to longer term. The recent sell-off of bonds, driven by weakening investor confidence, has spread to the high-yielding property stocks, driving a sharp performance downturn. This should contain upward pressure on commercial real estate values. Nonetheless, elevated investment risk remains inherent in aggressive acquisitive growth.

The newly enacted REIT legislation aims to standardise the regulatory and tax treatment of PLSs and Property Unit Trusts using internationally accepted practice. Any PLS registering as a REIT will be required to make a 'qualifying distribution' to the holders of its listed securities of at least 75% of its total distributable profits. Registration as a REIT is only currently available to listed entities. Such registration and listing is subject to the JSE Listing Requirements, including the condition that funds should have gross assets of at least R300m and cap on gearing of 60%. The new regulations are expected to improve management's flexibility, especially in terms of acquisitions and disposals. Under the new treatment, a qualifying REIT will be exempt from capital gains tax on the sale of immovable property, shares in other REITs and underlying subsidiaries. In addition, a qualifying REIT that pays out all of its distributable profits will effectively have no taxable income and will thus not be subject to income tax.

Financial performance

Attached are audited financials for the 2 years to F13, while brief comment follows hereafter. Auditors Ernst & Young provided an unqualified audit opinion on IPF's F13 results.

The strong acquisitive drive that has been maintained since the fund's inception has underlined robust top line growth. In this regard, rental income rose by 57% to R331m, underpinned by strong contributions from office and industrial properties. Stated after straight-line rental income adjustments, revenue climbed to R375m in F13, from R242m previously. Looking ahead, retail assets are expected to account for a higher proportion of income as certain assets make a full year contribution. Property expenses were up by 55%, a factor largely attributable to the fund's growing scale. Nonetheless, net rental income increased markedly to R316m in F13 (F12: R204m).

Triple net leases related to single-tenanted properties serve to contain operating expenses. In this regard, assessment rates and operating costs recovered from tenants comprised a low 5% and 3% of F13 revenue respectively (F12: 4%; 2%). Despite the higher retail exposure, the fund's cost to income ratio therefore remains much lower than that of larger funds, at 18% (F12: 18.2%).[1] Looking ahead, IPF is phasing in various initiatives, such as energy and water conservation projects, to contain tenants' all-in costs of occupation. This has become increasingly important, given double-digit utility and municipal cost escalations that will persist over the medium term. Strict credit control measures limited debtors impairments to 1.4% of total property expenses (F12: 3.1%), and arrears to less than 1% of total collectibles. This also helps to smooth out cash flows and improves the predictability of earnings. Stated before fair value movements, the operating margin was reported at a relatively stable 78.5% (F12: 79.2%), well above the 60% benchmark for highly rated property funds. While cost pressures are expected to derive from a shift in the segmental mix, management does not anticipate material margin compression in F14.

IPF reported unrealised gains of R118m on the property portfolio during the year (F12: R109m). However, a R197m debenture fair value adjustment (F12: R138m), coupled with a nominal loss related to interest rate swaps, drove an overall unrealised loss of R83m in F13, from R31m previously. IPF's debentures are adjusted to fair value to reflect the NAV attributable to debenture holders. Adjustments include the straight line rental revenue movement, capital items and other fair value changes on the fund's assets and liabilities. Stated after fair value movements, operating income equated to a reduced 56% of F13 revenue (F12: 66%).

Costs related to the fund's low debt levels were largely offset by interest income of R25m, and as such, IPF incurred a modest net finance charge of R14m in F13. Regardless of the funding mix that will be employed to finance future acquisitions, the interest outlay is likely to be well above these low levels in the medium term. The fund also generated R39m from the disposal of properties over the year. While further disposals were made in 1Q F14, the fund does not anticipate material cash flows to derive from the sale of properties, as it generally has a long term view towards its real estate assets. Overall, profit before debenture interest rose by 50% to R237m. This supported a distribution of nearly 100¢ per linked unit, up from 93¢ previously.

Cash generation remained robust, rising by 54% to R249m, on the back of the positive earnings impact of acquisitions. Despite a nominal R12m working capital absorption and the interest outlay, operating cash flows increased to R228m, from R174m previously. Since its inception, IPF had distributed a cumulative R238m to linked unitholders by FYE13, with the balance reflected as a current liability of R164m.

The fund made a R1.7bn cash outlay on acquisitions during F13, from R1.9bn expended in F12. This was financed by R1.5bn raised from the rights issue, as well debt raised during the year. Maintenance capex is largely predictable, and amounted to R37m in F13, up from a nominal R4m previously. The net cumulative cash outlay over the past 2 years was actually lower, at R28m. In F13, R19m spent on the enhancement of 4 Protea Place (an office property) largely accounted for the uptick in capex. The outlay on maintenance and refurbishments is not expected to rise materially in the short term. Amounts payable to linked unit holders, and

[1] Property expenses as a percentage of gross rental income. This excludes the asset management fee and other administration costs.

the cash consideration from F13 property disposals boosted the fund's year end cash balance to R399m. According to management, the proceeds from disposals were used to fund acquisitions post year end, reducing cash considerably. As PLS regulations required profits to be distributed, cash was historically kept at nominal levels, intermittently rising on account of dividends due to linked unit holders, and consideration from disposals.

Funding and liquidity profile

IPF's asset base is comprised almost entirely of investment properties. This has been largely financed by linked unitholder funds, with minimal recourse made to debt. Linked unitholders have demonstrated ongoing support for the fund's growth trajectory, following their rights during the year. This saw IPF's linked debenture holder interest more than double to R3.9bn by FYE13. The fund's aforementioned conversion to an all-equity structure will change the composition of capital in the short term, in line with the fund's REIT status.

IPF derives day-to-day liquidity from its operations, which generate sound monthly cash flows. In addition, a R500m bridging facility from Investec has been maintained, and has been renewed to 12 months, from 6 months previously. The facility is unsecured, and does not attract commitment fees. Part of the proceeds from the medium term, senior secured notes issued under the DMTN programme were used to redeem drawdowns amounting to R139m made during F12. As such, the facility was untapped at FYE13. Management also decided to create an evergreen SPV structure, to secure bank funding secured by a pool of bonded assets. Plans for the structure are at an advanced stage, with banking counterparties and the earmarked assets to serve as collateral already identified.

Senior notes: capital structure	Expiry	Coupon	R'm
IPF01	13-Apr-2015	3 month JIBAR+140 b.p.	134
IPF02	13-Apr-2016	3 month JIBAR+155 b.p.	40
IPF03	13-Apr-2017	3 month JIBAR+165 b.p.	50
IPF06	13-Apr-2017	Fixed: 8.8%	226
Total	-	-	**450**

IPF's senior secured notes are rated AA-$_{(ZA)}$ by GCR (stable outlook). For further information, subscribers are referred to GCR's Structured Finance Surveillance report on IPF's R450m Senior Secured Notes, dated March 2013. The notes are secured against 5 properties, which were valued at R948m at FYE13. This translates to a low ratio of encumbered investments of 23%, with an overcollateralisation of over 2x. Although according to international norms, property funds should show a more diverse range of long dated maturities, such instruments are not commonly utilised in the domestic market. Cognisance is also taken of the fund's low current utilisation of debt, in addition to the high proportion of unencumbered assets. Nonetheless, the aforementioned funding vehicle and further secured bond issuances will see the ratio of encumbered investment rise from current lows.

As at FYE13, the net loan-to-value ratio ("LTV") was negligible, while the gross LTV was reported at a low 11% (FYE12: 6%), comparing favourably to a 40% benchmark for highly rated funds. A 50% LTV covenant is contingent to the senior secured notes. Nonetheless, management does not intend to raise the LTV above 30% in the short term. Over the medium to longer term, IPF's LTV could be raised to a maximum of 40%, should debt become yield enhancing. Net debt to EBITDA was reduced to a low of 17% (gross debt to EBITDA: 153%), well below GCR's comfort level of not more than 400%. Earnings-based gearing ratio is projected to stay below this mark in the medium term, despite plans to leverage the balance sheet further.

IPF hedges at least 75% of its interest rate exposure through variable or fixed rate swaps. Hedges with 5 year maturities were used to fix the majority of IPF's variable rate exposure. In this regard, management estimated that a 100b.p rise in interest on its variable rate obligations would have reduced pre-distribution profit by R1.1m. Overall, the weighted effective interest rate on the fund's obligations was unchanged at 8.2% as at 1H F13. Net interest coverage was robust, at 21x (gross interest cover: 7.5x). While debt serviceability metrics should come down with further debt uptake, they should remain comfortably above the senior secured note covenant of 2x.

Liquidity

IPF currently relies on its Investec Bank facilities, which are deemed one of the competitive advantages deriving from group linkages, and are therefore viewed positively. Sustained shareholder support is evidenced by Investec's retention of its majority shareholding, synergies with its fellow subsidiaries that are involved in asset and property management, the raising of capital and the procurement of investment properties. Certain IPF assets are also tenanted by Investec subsidiaries, and the group has provided rental income guarantees for unlet properties sold to the fund. The decision to adopt a second funding structure will enhance the fund's liquidity, providing immediate access to capital through a revolving facility funded by at least one other bank. The DMTN programme was extended to R3bn, increasing the fund's access to capital markets.

Conclusion and rating rationale

In according the rating, GCR assessed IPF's portfolio and performance in relation to its position in the domestic property arena and international criteria. In this regard, the fund continued to demonstrate robust performance, underlined by a rapidly growing pool of properties with high occupancies and a long forward lease expiry profile. During the fund's short operational span, concentration risk in terms of income receivable and asset values has been managed down significantly, while sectoral diversification has shifted perceptibly. Going forward, IPF anticipates growth of 6%-8% on the base portfolio, supported by sustainable rental escalations and strong reversions. Robust acquisitive growth is planned for the medium term, with the property portfolio expected to double over the next 3 years.

Investec's majority shareholding underpins the fund's credit rating, as its continued capital and operational support provide critical competitive advantages.

Although GCR has not adopted a notching approach in assigning the rating, in view of IPF's small scale in comparison to Investec's broader operations, comfort is derived from the group's long term view towards its investment in the fund. IPF's strong linkages with Investec Property have facilitated the procurement of a pool of quality assets both from the group stable and from long standing clients. The company also lends its extensive experience in real estate towards the management of IPF's portfolio. Other group synergies underpin liquidity and fund raising. Broadly speaking, IPF taps into the group's intellectual capital, accessing systems and procedures, and benefiting from established relationships that provide it with a critical edge over other similar sized funds. GCR rates Investec Bank Limited $AA-_{(ZA)}$; $A1+_{(ZA)}$, while Investec Limited is secure-rated on an international scale.

GCR nonetheless remains cognisant of IPF's limited track record and scale relative to large, well-established domestic funds. While the portfolio is expected to grow substantially, heightened investment risk is inherent in this policy. With several funds also adopting growth mandates, this has placed upward pressure on the value of quality properties, increasing the risk of overpaying for assets.

Overall credit protection factors are expected to remain robust, with the LTV not expected to exceed the 30%-35% comfort range. Debt serviceability is projected to be robust in F14, with metrics expected to remain comfortably above covenants over the tenure of the fund's senior secured notes. Capital and liquidity support from Investec, the planned SPV and the DMTN programme provide a robust acquisitive platform for the fund. This is supported by the largely unencumbered property portfolio, which is indicative of above average recoveries for prospective unsecured note holders.

Investec Property Fund Limited

(Rand in millions except as noted)

Income Statement	Year ended : March	2012	2013
Rental income		211.6	331.4
Revenue (incl. straight line rental revenue adjustment)		*242.1*	*375.2*
EBITDA		**191.7**	**294.6**
Depreciation and amortisation		n.a	n.a
Operating income		**191.7**	**294.6**
Distributable earnings from associates and investments		0.0	0.0
Income from operations and investments		**191.7**	**294.6**
Net finance income (charges)		(3.0)	(14.0)
Finance cost capitalised		0.0	0.0
Fair value movements		(30.5)	(82.9)
Abnormal/exceptional items		0.0	39.1
Distribution to linked debenture holders		(158.0)	(236.6)
NPBT		**0.2**	**0.2**
Taxation charge		(0.0)	(0.1)
NPAT		**0.1**	**0.2**
Cash Flow Statement			
Cash generated by operations		**161.2**	**248.7**
Utilised to increase working capital		12.3	(11.8)
Net interest paid		0.7	(9.2)
Taxation paid		(0.1)	(0.0)
Cash flow from operations		**174.2**	**227.8**
Maintenance capex		0.0	0.0
Discretionary cash flow from operations		174.2	227.8
Distribution paid to linked debenture holders		(74.3)	(163.4)
Retained cash flow		**99.8**	**64.4**
Net expansionary capex		(1,926.2)	(1,726.2)
Investments and other		0.0	0.0
Proceeds on sale of assets/investments		0.0	240.6
Shares issued		1,700.0	1,496.4
Cash movement: (increase)/decrease		(4.6)	(394.2)
Borrowings: increase/(decrease)		130.9	319.1
Net increase/(decrease) in debt		**126.3**	**(75.1)**
Balance Sheet			
Ordinary shareholders interest		1.7	3.2
Outside shareholders interest		0.0	0.0
Linked debentures (capital)		1,836.4	3,940.0
Total shareholders' interest		**1,838.1**	**3,943.2**
Short term debt		130.9	0.0
Long term debt		0.0	450.0
Total interest-bearing debt		**130.9**	**450.0**
Linked debenture interest payable		0.0	0.0
Interest-free liabilities		113.1	246.2
Total liabilities		**2,082.0**	**4,639.3**
Fixed assets		0.0	0.0
Properties		2,065.4	4,187.0
Investments and advances		0.0	0.0
Cash and cash equivalent		4.6	398.7
Other current assets		12.1	53.6
Total assets		**2,082.0**	**4,639.3**
Ratios			
Cash flow:			
Operating cash flow: total debt (%)		133.1	50.6
Discretionary cash flow: net debt (%)		137.9	444.3
Profitability:			
Rental income growth (%)		n.a	56.6
EBITDA: revenues (%)*		79.2	78.5
Operating profit margin (%) *		79.2	78.5
EBITDA: average total assets (%)		10.2	9.3
ROaE (%)		8.9	8.2
Coverage:			
Operating income: gross interest (x)		31.8	7.5
Operating income: net interest (x)		63.5	21.0
Activity and liquidity:			
Days receivable outstanding (days)*		9.1	31.9
Current ratio (:1)		0.1	1.9
Capitalisation:			
Total debt: equity (%)		7.1	11.4
Net debt: equity (%)		6.9	1.3
Total debt: EBITDA (%)		68.3	152.7
Net debt: EBITDA (%)		65.9	17.4
Loan to value:			
Total debt: properties (%)		6.3	10.7
Net debt: properties (%)		6.1	1.2

*Calculated against rental income, inclusive of straight line rental revenue adjustments.

SALIENT POINTS OF ACCORDED RATINGS

GCR affirms that a.) no part of the rating was influenced by any other business activities of the credit rating agency; b.) the rating was based solely on the merits of the rated entity, security or financial instrument being rated; c.) such rating was an independent evaluation of the risks and merits of the rated entity, security or financial instrument; and d.) the validity of the rating is for a maximum of 12 months, or earlier as indicated by the applicable credit rating document.

Investec Property Fund Limited participated in the rating process via face-to-face management meetings, teleconferences as well as written correspondence. Furthermore, the quality of information received was considered adequate and has been independently verified where possible.

The credit rating/s has been disclosed to Investec Property Fund Limited with no contestation of the rating.

The information received from Investec Property Fund Limited and other reliable third parties to accord the credit rating included the latest audited annual financial statements, full year detailed budgeted financial statements, most recent year to date management accounts, corporate governance and risk framework, capital management policy, industry comparative data, regulatory framework and a breakdown of facilities available (including related counterparties). In addition, information specific to the rated entity and/or industry was also received.

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